

No. 77-952

Supreme Court, U. S.
FILED

JUL 25 1978

MICHAEL ROBAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1978

GROUP LIFE AND HEALTH INSURANCE COMPANY,
also known as BLUE SHIELD OF TEXAS, ET AL.,
PETITIONERS

v.

ROYAL DRUG COMPANY, INC., ETC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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INTEREST OF THE UNITED STATES

The issues in this case pertain to the scope of the exemption from the antitrust laws afforded to the business of insurance under the McCarran-Ferguson Act, 59 Stat. 33, as amended, 15 U.S.C. 1011-1015. The United States has the primary responsibility for

enforcing the antitrust laws. It therefore has a general concern that statutes creating exemptions from those laws not be interpreted more broadly than necessary to carry out the reasons for those exemptions. The extent to which the antitrust laws apply to the insurance industry is a matter of particular importance to the United States, because the scope of the exemption will affect prosecutorial decisions concerning anticompetitive conduct by insurance companies.

QUESTION PRESENTED

Whether an agreement between an insurance company and a pharmacist, designating the amount the insurance company will pay to the pharmacist for providing prescription drugs for which the insurance company must pay, is part of the "business of insurance" within the meaning of the McCarran-Ferguson Act.

STATUTES INVOLVED

Section 1 of the Sherman Act, 26 Stat. 209, as amended, 15 U.S.C. 1, provides in part:

Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal.

The McCarran-Ferguson Act, 59 Stat. 33, as amended, 15 U.S.C. 1011-1015, provides in pertinent part:

[Section 1] Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

[Section 2] (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the * * * Sherman Act, and the * * * Clayton Act, and * * * the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

* * *

[Section 3(b)] Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

STATEMENT

Petitioner Blue Shield offers an insurance policy (App. 51a-58a) that covers the risk that a policyholder will need to obtain prescription drugs. The

policy gives the insured person an option in obtaining such drugs. If an insured buys drugs from a "participating" pharmacy, the insured pays the pharmacy only \$2.00 (App. 55a). The \$2.00 is the total cost to the insured. If the insured buys drugs from a "nonparticipating" pharmacy, he pays the pharmacy the full price charged by the pharmacy and may obtain reimbursement from Blue Shield for 75 percent of the "result of the usual and customary charges for such covered drugs as determined by the Insurer, reduced by [\$2.00]" (App. 56a).

Blue Shield offered to enter into a Pharmacy Agreement (App. 59a-61a) with each licensed pharmacy in Texas. Each pharmacy entering into the agreement becomes a "participating" pharmacy. Under the Pharmacy Agreement, the pharmacy agrees to furnish drugs to Blue Shield's insureds for \$2.00, and Blue Shield agrees to reimburse the pharmacy for the pharmacy's cost of acquiring the drug.¹

¹ The agreement requires Blue Shield to pay the acquisition cost, plus a \$2.00 "professional dispensing fee," less the amount paid by the insured. The latter two items offset.

The following example may illustrate the operation of the insurance policy and the Pharmacy Agreement. Suppose the usual and customary retail price for a quantity of Drug X charged both by "participating" Pharmacy A and "non-participating" Pharmacy B is \$10.00, and the wholesale price (or acquisition cost) to both is \$8.00. If an insured buys Drug X from Pharmacy A, the insured pays \$2.00. Pharmacy A receives \$2.00 from the insured and \$8.00 from Blue Shield, or \$10.00 total. If an insured buys Drug X from Pharmacy B, the insured pays Pharmacy B \$10.00, and receives \$6.00 (75 percent of the difference between the retail

In 1969 Blue Shield filed its proposed prescription drug policy with the Texas State Board of Insurance for approval, as required by Texas law, and annexed to the filed policy the proposed Pharmacy Agreement (App. 352a-353a). After initial disapproval, the Board approved issuance of the policy in September 1969 (App. 370a-371a). The parties disagree about whether that action constituted a review and approval of the annexed Pharmacy Agreement (see Pet. Br. 2, 33-35; Resp. Br. in Opp. 11, 29-30).

In 1975 respondents, who operate non-participating pharmacies in Texas,² filed a complaint (App. 2a-11a) against petitioners (Blue Shield and three participating pharmacies), alleging that petitioners had violated Section 1 of the Sherman Act, 15 U.S.C. 1. The complaint charged that the Pharmacy Agreement is an agreement among petitioners to fix the price of drugs, to carry out a group boycott (by the insureds) of non-participating pharmacies, and to allocate territories and impose territorial restrictions (App. 8a-9a).

price and \$2.00) from Blue Shield. While Pharmacy B receives the same as Pharmacy A, the insured must pay \$4.00 for the drug and also must take steps to obtain reimbursement.

If the pharmacy's acquisition cost for the drug is \$5.00 rather than \$8.00, the situations of Pharmacy B and the insured are unchanged. But now Pharmacy A will receive only \$5.00 from Blue Shield, for a total of \$7.00.

² The record indicates that nine of the respondents also operate participating pharmacies in Texas (App. 14a, 19a, 31a, 50a).

The district court dismissed the complaint (App. 100a-116a), holding (among other things) that the challenged agreements are exempted from the federal antitrust laws by Section 2(b) of the McCarran-Ferguson Act, 15 U.S.C. 1012(b), because the agreements are part of the "business of insurance", are regulated by the State of Texas, and are not boycotts (*id.* at 108a-112a).

The court of appeals reversed (App. 117a-139a). It held that the Pharmacy Agreement is not part of the "business of insurance" because it "goes beyond Blue Shield's obligation as an insurer and places the firm in the business of providing products and services" (App. 129a). Although the Pharmacy Agreement is "somewhat related to the business of insurance * * * [t]he relationship * * * is so attenuated that it must be subject to the antitrust laws" (App. 132a).³

SUMMARY OF ARGUMENT

A. There is no issue before this Court concerning the lawfulness of petitioners' agreements or practices under the antitrust laws. Although petitioners and most of the *amici* supporting them argue that insurance plans and provider agreements such as theirs greatly benefit the consumer, those arguments are

³ Having found that the Pharmacy Agreements are not part of the business of insurance, the court did not reach the other questions decided by the district court. It observed, however, that "there is no * * * indication that the activities complained of are considered the business of insurance by the State" (App. 135a).

irrelevant because there has been no determination that petitioners' plans and practices violate the antitrust laws. As a general matter, moreover, antitrust principles would not preclude the offering of prepaid health plans that use insurer-provider agreements.

Whatever the likelihood of respondents' ultimate success on the merits, however, respondents' complaint formally alleges antitrust violations, and those allegations must be assumed to be true for purposes of ruling on petitioners' motion to dismiss. The issue in the case is whether, on that assumption, the challenged agreements and practices of petitioners are part of the "business of insurance" that Section 2(b) of the McCarran-Ferguson Act exempts from the antitrust laws. Because provider agreements of the kind challenged here could be the vehicle for agreements and practices that violate the antitrust laws, that issue is important for antitrust policy and enforcement.

B. Several considerations support the court of appeals' conclusion that the provider agreements in this case are not part of the "business of insurance" within the meaning of Section 2(b).

1. The analysis of the issue must start from the premise, stated many times by this Court, that exemptions from the antitrust laws must be narrowly construed. See, *e.g.*, *Abbott Laboratories v. Portland Retail Druggists Association, Inc.*, 425 U.S. 1, 11-12.

2. The ordinary understanding of the "business of insurance" is the underwriting of risk and the

relationship between the insurer and the persons whose risks are insured. *Securities and Exchange Commission v. Variable Annuity Co.*, 359 U.S. 65. Blue Shield's agreements with various pharmacies are not the underwriting of risk; they are merely contracts for the purchase of goods and services at a specified price. The fact that they may be related to Blue Shield's insurance policies does not clothe them with the same status. Everything an insurance company does to make money or to contain or reduce its costs can be said to relate to its insurance, but neither the common understanding of the "business of insurance" nor the legislative intent would include every such activity within the scope of that term.

3. The legislative history and this Court's opinion in *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453, demonstrate that the "business of insurance" was understood by Congress to involve the underwriting of risk and the relationships and transactions between insurance companies and their policyholders. Nothing in that history suggests that Congress intended to exempt agreements or transactions between insurance companies and entities outside the insurance industry. Petitioner's arguments that the Pharmacy Agreements should be regarded as part of the business of insurance because they affect Blue Shield's costs (and therefore the amount of premiums charged) and enhance its status as a reliable insurer are beside the point. If effect on insurance were the touchstone, the exemption would

apply to "insurers." It is not written so broadly, however. The "business of insurance" is less than the entire "business of insurers."

An agreement between an insurance company and a non-insurance entity may or may not violate the antitrust laws, depending on its purpose or effect, but it is not exempt from such laws as part of the "business of insurance." If the purpose or effect of such an agreement is to restrain competition in markets other than the insurance market, nothing in the McCarran-Ferguson Act or its legislative history suggests that Congress intended to immunize it from the antitrust laws.

4. These arguments are supported by this Court's decisions concerning the analogous antitrust exemption for labor agreements. It is well established that labor agreements about wages and other conditions of employment are, as a general matter, exempt from the antitrust laws. But where the evidence shows that such an agreement is a device designed to restrain competition among employers or to affect markets other than the labor markets, it has no antitrust immunity. See, e.g., *United Mine Workers v. Penn-ington*, 381 U.S. 657. The same principles support the conclusion that an agreement between an insurance company and a firm selling goods or services is not exempt from the antitrust laws.

ARGUMENT

AGREEMENTS BETWEEN INSURERS AND PROVIDERS OF SERVICES ARE NOT PART OF THE "BUSINESS OF INSURANCE"

A. The Court Need Not Decide Whether The Agreements Violate The Antitrust Laws

This case, in its present posture, does not require the Court to decide whether the Pharmacy Agreements violate the antitrust laws. The only question is one of immunity from the antitrust laws, and if this Court should hold that there is no immunity the lower courts would then be required to consider whether the practices are lawful. It should go without saying that agreements and practices can be non-immune and still be perfectly lawful.

Petitioners and *amici* supporting them devote most of their briefs to arguing that provider agreements such as the Pharmacy Agreements are integral to prepaid health insurance programs and that they are reasonable and in the interest of the consumer. Respondents argue that the Pharmacy Agreements are price-fixing and violate the antitrust laws in other ways. These arguments, however important they may be in determining questions of substantive antitrust law, are irrelevant to the immunity issue.

As a general matter, however, antitrust principles would not preclude the offering of prepaid health in-

surance programs that use insurer-provider agreements. For example, the pleadings in this case indicate that the Pharmacy Agreements are bilateral contracts for the purchase of goods and services by Blue Shield. Blue Shield has offered to purchase drugs and pharmacy services from any pharmacy that will accept acquisition cost plus \$2.00. Unless respondents could establish that some conspiracy among pharmacies is at work the Pharmacy Agreements would not amount to "price fixing." Transactions at a set price, through a series of voluntary bilateral contracts, are not price fixing even though large numbers of sellers of services may be involved. *Theatre Enterprises, Inc. v. Paramount Film Distributing Corp.*, 346 U.S. 537; *Dahl, Inc. v. Roy Cooper Co.*, 448 F.2d 17 (C.A. 9). Cf. *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320.

For all that appears on the face of the complaint, Blue Shield has acted as an agent of the policyholders to secure drug distribution services at the lowest possible cost. Blue Shield has offered to deal directly with any pharmacy willing to accept a low price for its services. Any pharmacy that can distribute drugs for \$2.00 or less per prescription could accept Blue Shield's offer. This process serves to help the policyholders find low-overhead pharmacies with which to deal. Moreover, it provides pharmacies with incentives to reduce their distribution costs in order to be

able to take advantage of Blue Shield's offer and still make a profit.

Respondents' principal complaint seems to be that the series of Pharmacy Agreements—which make it advantageous for policyholders to patronize pharmacies that are willing to take only \$2.00 for distribution services—prevents them from obtaining as much money as they need or desire (App. 7a-8a; Br. in opp. 5-10). That kind of complaint does not state an antitrust violation. Nothing in the antitrust laws requires drug purchasers (or Blue Shield acting as their purchasing agent) to offer the greater compensation necessary to satisfy less efficient pharmacies or suppliers interested in providing expensive but unwanted services at the point of sale. To the contrary, antitrust policy seeks to preserve to consumers the opportunity to obtain a better deal. Its goal is consumer welfare, not competitor welfare. See *National Society of Professional Engineers v. United States*, No. 76-1767, decided April 25, 1978; *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36; *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488; *Brown Shoe Co. v. United States*, 370 U.S. 294, 320.⁴ Indeed, in 1968 the Department of Justice issued a business review letter indicating that agreements between individual insurers and individual providers, to carry out a prepaid insurance plan, do not violate the antitrust laws

⁴ See also 1 Areeda and Turner, *Antitrust Law* ¶¶ 103-113 (1978); 3 *id.* at ¶ 732.

(Department of Justice Clearance letter, January 15, 1968, reproduced at App. E of Amicus Br. of the Blue Shield Association).⁵

Nevertheless, the complaint in this case at least formally sets out the elements of a violation of the antitrust laws, and in passing on the immunity arguments it is necessary to assume that the Pharmacy Agreements are combinations or conspiracies in restraint of trade.⁶ The dispositive issue is whether, on

⁵ Several portions of the court of appeals' opinion appear to characterize petitioners' activities as coercive or as "price fixing" (e.g., App. 127a, 137a). It may be that the court was simply assuming, as it was required to do, that respondents ultimately could make out a violation of the antitrust laws. To the extent the court of appeals was indicating that the conduct described in the complaint is a *per se* violation of the Sherman Act, we cannot agree with that view for the reasons stated in the text.

⁶ The most troublesome opportunity for a restraint of trade would exist if the providers of goods and services also controlled the insurance companies. If, for example, pharmacies controlled Blue Shield, and if Blue Shield also possessed substantial power in the insurance market, the providers could use the insurance business to make or carry out their agreement in restraint of trade. They might agree to increase prices and carry out the agreement through their control of the insurers. Although such a development would be of considerable concern to the United States and to the Federal Trade Commission, the complaint in the present case does not allege that the pharmacies control Blue Shield and can require it to act in the interest of pharmacies rather than policyholders.

Provider agreements might violate the antitrust laws even in the absence of an allegation of "provider control." It is possible,

that assumption, the Pharmacy Agreements are exempt from antitrust scrutiny as part of the "business of insurance" within the meaning of Section 2(b) of the McCarran-Ferguson Act. We submit that they are not.

for example, that evidence might establish that the participating pharmacies conspired among themselves to obtain a price for distribution higher than they otherwise could obtain. In that event, however, Blue Shield and the insureds would be the victims of the conspiracy, and they would join it only if faced with a united group of providers. In other words, an effective provider conspiracy could not succeed unless it could obtain the support of most pharmacists, because otherwise non-members of the cartel would offer competitive prices and attract the business. The complaint here does not allege facts sufficient to show an antitrust violation under this theory.

There would be genuine antitrust concern, too, if it could be established that the participating pharmacies are using the Pharmacy Agreements to engage in predatory pricing. Again, however, Blue Shield would not participate in that conspiracy, which would work to the long-run detriment of the insureds, unless confronted with an agreement involving a substantial proportion of the pharmacies. Moreover, there has been no allegation that the Pharmacy Agreements entail sales at less than marginal cost (see 3 Areeda and Turner, *supra*, at ¶¶ 710-722), and the complaint thus does not set out an essential element of predatory pricing. It also would be significant to a predatory pricing case whether new pharmacies could enter the market to replace pharmacies that had been driven out. If there were prompt entry, the predators could not capture for long the increased market share that is necessary to make predation profitable. The complaint does not allege that barriers to entry would prevent renewed competition from overcoming the hoped-for effects of predation.

B. The Pharmacy Agreements Are Contracts For The Purchase And Sale Of Distribution Services

The McCarran-Ferguson Act does not define the "business of insurance," and the legislative history does not provide a definitive explanation of the phrase. *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453, 458. Several considerations, however, support the court of appeals' conclusion that the Pharmacy Agreements are not part of the "business of insurance."

1. Antitrust exemptions must be narrowly construed

Analysis of the question must begin with the general principle that exemptions from the antitrust laws are to be narrowly construed and limited to the scope clearly defined by Congress. *Abbott Laboratories v. Portland Retail Druggists Association, Inc.*, 425 U.S. 1, 11-12; *Federal Maritime Commission v. Seatrain Lines, Inc.*, 411 U.S. 726, 733. Cf. *National Broiler Marketing Association v. United States*, No. 77-117, decided June 12, 1978; *Maryland and Virginia Milk Producers Association, Inc. v. United States*, 362 U.S. 458, 464-467. It would be inappropriate to conclude that the competitive restraints alleged to exist here are exempt from the antitrust laws unless the purpose of the McCarran-Ferguson Act or the clear legislative history requires that result.

2. The provider agreements do not pool or spread risk

Because there is no statutory definition of the "business of insurance," it is appropriate to consider first the common and ordinary meaning of the term.

See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 and n. 19. And, as commonly understood, the business of insurance does not include the kind of provider agreements involved in this case.

In common parlance, the "business of insurance" is the underwriting of risk and the relationships and transactions between the insurance company and the persons whose risks are insured. This Court so held in *Securities and Exchange Commission v. Variable Annuity Co.*, 359 U.S. 65. In that case a company had issued annuities, the benefits of which depended on the success or failure of a portfolio of stocks in which the premiums were invested. Because the risk thus fell on the annuitant and not the company, the Court held that the annuities were not part of the "business of insurance" that the McCarran-Ferguson Act exempted from Commission regulation: "There is no true underwriting of risks, the one earmark of insurance as it has commonly been conceived of in popular understanding and usage." 359 U.S. at 73 (footnote omitted).

The Pharmacy Agreements are not an underwriting of risk. They are merely contracts for the purchase of drugs and distribution of services for Blue Shield's customers. They are not part of the business of insurance "as it has commonly been conceived of in popular understanding and usage."

⁷ In a sense, of course, every contract for the sale of goods or services in the future at a specified price protects the parties against the risk of future fluctuations in the market price, but that is clearly not the kind of underwriting of risk that is commonly understood to constitute, or is in any way peculiar to, the "business of insurance."

There is an important distinction between risk *underwriting* and risk *reduction*. The Pharmacy Agreements reasonably could be viewed as a method of reducing Blue Shield's risk. By agreeing with pharmacies on the price it will pay for drugs, Blue Shield has reduced the total amount it must pay to fulfill its risk-related obligations to its policyholders. But this device does not spread risk more widely or reduce the role of chance events (illnesses, *e.g.*) in Blue Shield's business. The Pharmacy Agreements may eliminate some risk, but they do not underwrite risk.

Many practices that could be undertaken by insurance companies and by other persons could affect the total amount of risk. For example, an automobile manufacturer that invents a more effective bumper could make safer cars, reducing the loss caused by accidents. If the large insurance companies then agreed with the principal automobile manufacturers that the safer bumper would be installed on every car, whether or not the consumer wanted the new bumper, this would reduce still further the loss caused by accidents. The decreased loss would affect, perhaps significantly, the premiums for automobile insurance. But no one would think that this process of invention, followed by a combination or agreement to sell only cars equipped with the new bumper, was part of the business of insurance. The fact that the agreement involved manufacturers and insurers, rather than manufacturers alone, would not affect its nature. The explanation of this intuitive reaction is that the invention and agreement—no matter how desirable to

society—simply reduces loss and risk. It does not spread risk more widely or more effectively. It is risk reduction rather than risk underwriting.* The same principle applies here: the Pharmacy Agreements reduce but do not spread risk, and they are thus not part of the “business of insurance.”

The fact that transactions or agreements may have some relationship to a company’s insurance business or its insurance policies does not make all of those transactions or agreements part of the business of insurance. Insurance companies engage in many transactions that are more or less related to, or even necessary for, its insurance functions. They contract with printers to obtain insurance policy forms, lease buildings to carry out their business, and lend money to raise the funds necessary to carry out the promises made in their policies. But none of those activities would commonly or reasonably be regarded as the “business of insurance.” Moreover, as we now discuss, there is no reason to conclude that Congress intended to exempt from the antitrust laws an insur-

* Similarly, an insurance company might conduct medical research designed to find a way to prevent cancer or to cure the common cold. It might make discoveries that would allow large savings in the cost of medical care or obliterate the need to purchase many prescription drugs that are now sold. Such discoveries would have considerable effects on insurance rates and on the terms of policies. But no one would argue that this medical research—or a contract between an insurance company and a laboratory to conduct medical research—is part of the “business of insurance.” It is part of the business of medicine, and although it may reduce risk it would not underwrite risk.

ance company’s participation in a price-fixing agreement among printers or building owners or other lenders.

3. *The legislative history indicates that ancillary business agreements of insurers are not part of the “business of insurance”*

a. Although the legislative history of the McCarran-Ferguson Act does not provide a definitive explanation of the term “business of insurance,” that history, which this Court has reviewed on several occasions, does demonstrate that Congress’ concern was with the relationship between the insurer and the insured, and with preserving state regulation of that relationship. Nothing in the legislative history suggests that Congress intended to immunize relationships or transactions between insurance companies and other entities (such as pharmacies) outside the insurance industry, even though such relationships or transactions may be more or less “related” to the insurance function (as they always would be to some degree when one party is an insurance company).

Securities and Exchange Commission v. National Securities, Inc., *supra*, is this Court’s most extensive consideration of the legislative history of the Act. The Court held that the Securities and Exchange Commission was not precluded from seeking to dissolve a merger between two insurance companies that had been approved by the state insurance director but that allegedly violated the federal securities laws. The Court concluded that state regulation of insur-

ance company mergers designed to protect stockholders was not regulation of the "business of insurance" within the meaning and intent of the McCarran-Ferguson Act,^{*} and the Court's discussion of the legislative history provides significant guidance for the resolution of the issue in this case.

The Court first noted (393 U.S. at 458) that the McCarran-Ferguson Act was passed in response to *United States v. South-Eastern Underwriters Association*, 322 U.S. 533, in which this Court had held that insurance transactions were transactions in interstate commerce and thus subject to the antitrust laws. As a result of fears that *South-Eastern Underwriters* might displace or invalidate traditional state regulation and taxation of the insurance industry, Congress enacted the McCarran-Ferguson Act "to give support to the existing and future state systems for regulating and taxing the business of insurance." *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408, 429. See also *St. Paul Fire & Marine Insurance Co.*

^{*} In that case the issue concerned the application of the provision in Section 2(b) that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance * * *." This case concerns the portion of Section 2(b) that relates specifically to the Sherman, Clayton and Federal Trade Commission Acts and provides that those Acts "shall be applicable to the business of insurance to the extent that such business is not regulated by State law." While there are differences between the operation of the two provisions that are not relevant here, the term "business of insurance" has the same scope in both provisions, and the analysis of *National Securities* is therefore pertinent.

v. Barry, No. 77-240, decided June 29, 1978, slip op. 6-7.

The Court then stated that (393 U.S. at 459-460; emphasis in original):

it is relatively clear what problems Congress was dealing with. Under the regime of *Paul v. Virginia*, *supra*, States had a free hand in regulating the dealings between insurers and their policyholders. Their negotiations, and the contract which resulted, were not considered commerce and were, therefore, left to state regulation. The *South-Eastern Underwriters* decision threatened the continued supremacy of the States in this area. The McCarran-Ferguson Act was an attempt to turn back the clock, to assure that the activities of insurance companies in dealing with their policyholders would remain subject to state regulation.

* * * * *

Given this history, the language of the statute takes on a different coloration. The statute did not purport to make the States supreme in regulating all the activities of insurance companies; its language refers not to the persons or companies who are subject to state regulation, but to laws "regulating the business of insurance." Insurance companies may do many things which are subject to paramount federal regulation; only when they are engaged in the "business of insurance" does the statute apply. Certainly the fixing of rates is part of this business; that is what *South-Eastern Underwriters* was all about. The selling and advertising of policies, *FTC v. National Casualty Co.*, 357 U.S. 560 (1958), and

the licensing of companies and their agents, cf. *Robertson v. California*, 328 U.S. 440 (1946), are also within the scope of the statute.

The Court concluded (393 U.S. at 460):

Congress was concerned with the type of state regulation that centers around the contract of insurance, the transaction which *Paul v. Virginia* held was not "commerce." The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement—these were the core of the "business of insurance." Undoubtedly, other activities of insurance companies relate so closely to their status as reliable insurers that they too must be placed in the same class. But whatever the exact scope of the statutory term, it is clear where the focus was—it was on the relationship between the insurance company and the policyholder. Statutes aimed at protecting or regulating this relationship, directly or indirectly, are laws regulating the "business of insurance."

The legislative history confirms what the Court stressed in *National Securities*—that Congress' concern was with the relationship between the insurance company and the insured. First, the debates and committee reports on the Act and earlier versions of it consistently reflect the understanding that the underwriting of risk is the "business of insurance"; Congress wanted to preserve the states' traditional regulation of that function. See 90 Cong. Rec. 6544 (1944) (remarks of Rep. Clason); 90 Cong. Rec. 6526 (Rep. Hancock); H.R. Rep. No. 873, 78th Cong.,

1st Sess. 8-9 (1943);¹⁰ S. Rep. No. 1112, 78th Cong., 2d Sess. 6 (1944). Second, Congress rejected several proposed bills that would have more broadly exempted from the antitrust laws "the business of insurance or * * * acts in the conduct of that business * * *."¹¹

¹⁰ For example, the House Judiciary Committee Report on H.R. 3270, a forerunner of the McCarran-Ferguson Act, recognized that insurance is the "distribution of risk according to hazard, experience, and the laws of averages." H.R. Rep. No. 873, 78th Cong., 1st Sess. 8-9 (1943). These factors, the report stated, "are not within the control of insuring companies in the sense that the producer or manufacturer may control cost factors." *Id.* at 9.

These conclusions were echoed in S. Rep. No. 1112, 78th Cong., 2d Sess. 6 (1944), which viewed insurance as a personal promise of indemnity, and thus "something quite different from the ordinary commercial transaction."

¹¹ In anticipation of the *South-Eastern Underwriters* decision, three identical bills were introduced in the 78th Congress, which would have made the Sherman and Clayton Acts inapplicable to the business of insurance: H.R. 3269, H.R. 3270 and S. 1362, 78th Cong., 1st Sess. (1943). These bills provided that nothing in the Sherman or Clayton Acts "shall be construed to apply to the business of insurance or to acts in the conduct of that business or in any wise to impair the regulation of that business by the several States." None of these bills was enacted. S. Rep. No. 1112, 78th Cong., 2d Sess. (1944); H.R. Rep. No. 873, 78th Cong., 1st Sess. (1943). The bill that became the McCarran-Ferguson Act, S. 340, was introduced early in the 79th Congress and was reported favorably by the Senate Judiciary Committee on January 24, 1945. S. Rep. No. 20, 79th Cong., 1st Sess. (1944). At approximately the same time Rep. Walter introduced a similar measure (H.R. 1973, 79th Cong., 1st Sess. (1945)), which was reported favorably by the House Judiciary Committee on February 8, 1945. The McCarran-Ferguson Act was amended on the floor of the Senate and passed as amended. It was referred to the House Judiciary Committee, which struck the entire substance

Third, the limits on the scope of the "business of insurance" are reflected in the comments of the Association of Insurance Commissioners, whose views (as petitioners agree, Pet. Br. 31 n. 28) are particularly significant because the Act evolved from a draft bill the Association submitted to Congress. See 91 Cong. Rec. 483 (1945) (remarks of Sen. O'Mahoney). The Association's draft bill specifically listed the activities that the Association believed warranted exemption from the antitrust laws, including agreements concerning rates, forms and rules, agents' commissions, reinsurance, and the pooling of statistics. 90 Cong. Rec. A4406 (1944).¹² All of the listed activities concerned agreements within the insurance industry, agreements that related directly to the pooling of risk and the sale of policies. Nothing in the Association's draft or supporting statements indicated an understanding that ancillary purchases of goods and serv-

of the bill, substituted the language in the Walter bill, and reported S. 340 as amended. H.R. Rep. No. 143, 79th Cong., 1st Sess. (1945). This bill was passed by the House. A Conference Committee added Section 2(b) and reported the bill. H.R. Conf. Rep. No. 213, 79th Cong., 1st Sess. (1945). This bill passed both Houses of Congress and was signed by President Roosevelt on March 9, 1945.

¹² In his statement before the Joint Hearing of the Subcommittees of the Committee on the Judiciary, on S. 1362, H.R. 3269, and H.R. 3270, 78th Cong., 1st Sess. 219 (1943), A. V. Gruhn, then Manager of the American Mutual Alliance of Chicago, expressed the same views concerning what constitutes insurance and why it required special exemption from the antitrust laws. Edward L. Williams, the President of the Insurance Executives Association, expressed identical views. *Id.* at 259, 266.

ices by insurance companies were intended to receive antitrust immunity. See 90 Cong. Rec. A4403-A4408 (1944).

Finally, the views of Mr. Chief Justice Stone, dissenting in *South-Eastern Underwriters*, are pertinent because the McCarran-Ferguson Act was enacted to overrule that case. Mr. Chief Justice Stone stated that although, in his view, the issuance of insurance was not interstate commerce subject to the antitrust laws, use of insurance contracts to restrain commerce in other goods or services would be subject to antitrust enforcement (322 U.S. at 570-571):

If contracts of insurance are in fact made the instruments of restraint in the marketing of goods and services in or affecting interstate commerce, they are not beyond the reach of the Sherman Act more than contracts for the sale of commodities * * *.

It is not unreasonable to ascribe the same view to the 78th Congress.¹³

In sum, the legislative history of the McCarran-Ferguson Act and this Court's decision in *National Securities* demonstrate that Congress sought to preserve state regulation of the relationships and trans-

¹³ The remarks of Attorney General Biddle, testifying in the Joint Hearing on S. 1362, H.R. 3269, and H.R. 3270 before the Subcommittees of the Committee on the Judiciary, 78th Cong., 1st Sess. 41-42 (1943), cited by petitioners (Br. 22-23), do not indicate that he considered insurer-provider agreements part of the business of insurance. Rather, the Attorney General's remarks merely indicate a belief that prepaid health plans are the business of insurance, a view that is not now in dispute.

actions between insurance companies and their policyholders. Unquestionably, as the Court noted in *National Securities*, certain other activities of insurance companies may be "relate[d] so closely to their status as reliable insurers that they too must be placed in the same class" (393 U.S. at 460).¹⁴ But there is no basis in the legislative history or policies of the Act for concluding that an agreement between an insurance company and a supplier of goods or services other than insurance is part of the "business of insurance" or is something Congress wanted to exempt from the antitrust laws.¹⁵

¹⁴ As one court of appeals has said, "[t]he question is ultimately one of line-drawing, based on the facts of the individual case." *Proctor v. State Farm Mutual Automobile Insurance Co.*, 561 F. 2d 262, 268 (C.A.D.C.), petition for a writ of certiorari pending, No. 77-580. One example of the "business of insurance" not directly involving insurer-insured relationships, would be agreements and transactions between insurance companies and independent insurance agents relating to sales of insurance by those agents. While such agreements or transactions do not themselves concern the relationship between the insurer and the insured, they are plainly closely related. Such agreements or transactions are readily distinguishable from provider or supplier agreements, since an insurance agent sells insurance, and a provider or supplier sells other goods or services.

¹⁵ What is more, the legislative history indicates that Congress believed that traditional state regulation of the insurer-insured relationship would adequately protect the public, and Section 2(b) accordingly exempts the "business of insurance" from the antitrust laws "to the extent that such business is regulated by State law." On the basis of the expressed congressional intent to defer to state regulation of that business, courts have held that state regulation of the business

b. Petitioners argue that Blue Shield's Pharmacy Agreements are part of the "business of insurance" because they involve the type of insurance policy Blue Shield issues, its reliability, interpretation and enforcement, and Blue Shield's status as a reliable insurer (Pet. Br. 21-31). They maintain that the Pharmacy Agreements enable Blue Shield to fulfill its obligations to its policyholders and to make sure that they receive benefits at the lowest possible price.

These arguments prove too much, for they would encompass almost everything an insurance company does. For example, an insurance company that agrees with other lenders to fix lending rates could, under petitioners' arguments, reasonably claim that the purpose of the agreement was to keep premium charges down and to ensure that the company remained sound

need not be affirmative or effective to supplant the federal antitrust laws. *Federal Trade Commission v. National Casualty Co.*, 357 U.S. 560, 564; *Dexter v. Equitable Life Assurance Society*, 527 F.2d 233 (C.A. 2); *Crawford v. American Title Insurance Co.*, 518 F.2d 217, 219 (C.A. 5). Accordingly, if the "business of insurance" were construed broadly to include activities on the periphery of that business, there would be a substantial danger that the public would lack any effective protection from deceptive or anticompetitive practices, contrary to Congress' expectations and premise in enacting the McCarran-Ferguson Act. This consideration counsels that, in close cases, doubts be resolved against including particular activities within the "business of insurance" and reinforces the traditional rule that exceptions to the antitrust laws should be narrowly construed (see page 15, *supra*).

enough to pay insurance obligations.¹⁶ The same purposes and justifications could be advanced for any other anticompetitive conspiracy between an insurance company and a group of suppliers that redounded to the benefit of the insurance company.¹⁷ But, as this Court recognized in *National Securities*, "[i]nsurance

¹⁶ The fact that the insurance policy itself makes reference to "participating pharmacies," and thus implicitly contemplates the subsequent arrangements between the insurer and the pharmacies, does not affect this case. If, for example, an insurance policy made reference to a proposed price-fixing agreement among the insurer and other lenders and asserted that the proposed agreement was for the purpose of enhancing the insurer's ability to pay claims on the policy, there is no reason to assume that the mere reference in the policy would immunize the price-fixing agreement.

¹⁷ We emphasize once more that the issue of the lawfulness of the agreement should not be confused with the issue in this case. Since there may be anticompetitive agreements or practices between an insurance company and entities outside the insurance industry in which the insurance company would have an incentive to engage, the principle that the "business of insurance" exemption should be narrowly construed is important to antitrust policy.

Indeed, petitioners (Br. 39) and several *amici* (UAW and AFL-CIO Br. 15-19; Motor Vehicle Manufacturers Association Br. 18-19) appear to recognize that provider agreements do not necessarily violate the antitrust laws. They argue that the mere possibility of suits, however unmeritorious, will inhibit socially desirable prepayment insurance plans. This Court, however, recently rejected a similar claim for antitrust exemption based on the argument that the mere threat of unmeritorious lawsuits would adversely affect the operations of municipal governments. *City of Lafayette v. Louisiana Power & Light Co.*, No. 76-864, decided March 29, 1978.

companies * * * do many things" (393 U.S. at 459), and it was not the intent of the McCarran-Ferguson Act to exempt everything an insurance company does from the antitrust laws.¹⁸ See also pages 17-18, *supra*, which discuss the important difference between the risk underwriting and risk reduction.

c. Most of the federal courts that have dealt with provider agreements similar to petitioners' have concluded that, because such agreements may affect the premiums charged and consequently may affect the

¹⁸ Petitioners also argue (Br. 31-35) that the Pharmacy Agreements are part of the "business of insurance" because, petitioners claim, they are regulated by the Texas State Board of Insurance and because the Texas Attorney General has opined that prescription drug insurance "plans" (which petitioners claims include provider agreements) constitute the "business of insurance." Respondents dispute that Texas exercises any jurisdiction over the Pharmacy Agreements and that the State has authoritatively spoken on the issue (Br. in Opp. 11, 29, 30), and the court of appeals held that "there is no * * * indication that the activities complained of are considered the business of insurance by the State" (App. 135a). While the court of appeals' view seems to us correct, the issue is not significant, because, as petitioners concede (Br. 31 n. 28), the meaning of the "business of insurance" is a federal question. A state cannot authorize a violation of the federal antitrust laws, or confer an antitrust immunity, simply by encouraging or approving private anticompetitive conduct. *Cantor v. Detroit Edison Co.*, 428 U.S. 579; *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384.

We do not understand petitioners to claim that the State has dictated the terms of the Pharmacy Agreement in a way that would provide a defense under the doctrine of *Parker v. Brown*, 317 U.S. 341. There seems little basis for such a claim, which, in any event, would be a matter to be determined at a trial on the merits.

insurer's reliability, they are part of the "business of insurance."¹⁹ To the extent those decisions rest on the proposition that agreements or practices come within the business of insurance when they can be said to affect premium charges or the financial soundness of the insurance company, we disagree for the reasons we have previously stated.

It may be useful, however, to discuss *Proctor v. State Farm Mutual Automobile Insurance Co.*, 561 F. 2d 262 (C.A.D.C.), petition for a writ of certiorari pending, No. 77-580, because that decision illustrates the prevailing rationale of the lower courts. Certain auto body repair shops sued five insurers, claiming that the insurers had violated the Sherman Act (1) by agreeing among themselves to pay their insured's claims for auto repairs on the basis of an agreed formula involving the "prevailing labor rate" and (2) by agreeing with certain repair shops to fix the price of auto repairs. The court concluded that both

¹⁹ See *Proctor v. State Farm Mutual Automobile Insurance Co.*, 561 F. 2d 262 (C.A.D.C.), petition for a writ of certiorari pending, No. 77-580; *Doctors, Inc. v. Blue Cross of Greater Philadelphia*, 557 F. 2d 1001 (C.A. 3); *Travelers Insurance Co. v. Blue Cross of Western Pennsylvania*, 481 F. 2d 80 (C.A. 3); *Frankford Hospital v. Blue Cross of Greater Philadelphia*, 417 F. Supp. 1104 (E.D. Pa.), affirmed, 554 F. 2d 1253 (C.A. 3); *Anderson v. Medical Service of the District of Columbia*, 1976-1 CCH Trade Cases ¶ 60,884 (E.D. Va.), affirmed, 551 F. 2d 304 (C.A. 4); *Manasen v. California Dental Services*, 424 F. Supp. 657 (N.D. Cal.). But cf. *Battle v. Liberty National Life Insurance Co.*, 493 F. 2d 39 (C.A. 5), certiorari denied, 419 U.S. 1110; *Hill v. National Auto Glass*, 293 F. Supp. 295 (N.D. Cal.).

types of the alleged agreements are part of the "business of insurance," although it confessed "somewhat more difficulty with [the] allegations of vertical arrangements with preferred shops and a group boycott of non-cooperative shops." 561 F. 2d at 267.

We agree with the court's conclusion about the horizontal agreements among the insurance companies. They are wholly intra-insurance industry agreements concerning the extent to which particular claims would be paid. The formula for the payment of insurance claims is an integral part of any contract of insurance, because it determines how much risk is involved, and how much of the risk will be assumed by the insurer. Such agreements among insurers are no different in substance from agreements on the premiums to be charged,²⁰ and the McCarran-Ferguson Act's chief purpose was to leave such matters exclusively to state regulation. It may be, of course, that the mechanism chosen to enforce the agreement might amount to "boycott, coercion, or intimidation," in which case the antitrust laws would apply (see *St. Paul Fire & Marine Insurance Co. v. Barry*, *supra*, slip op. 12-13 and n. 18), but the agreement is still part of the business of insurance.

We do not agree, however, with the court's conclusion that vertical agreements between insurance com-

²⁰ To take the simplest example, an agreement between two life insurance companies to charge a \$10 premium for every \$1000 of death benefits is the same thing as an agreement to pay \$1000 of death benefits for every \$10 of premiums collected from the deceased.

panies and auto repair shops are also part of the business of insurance if they can be said to have a "vital impact on [the insurers' insurance] rates * * *." 561 F. 2d at 270. That principle would exempt almost any kind of anticompetitive practice, if it could be shown that the practice were sufficiently advantageous to the company that it could pass along the advantage to its insureds in the form of lower premiums.

Although any definition of the "business of insurance" requires a certain amount of "line-drawing" (563 F.2d at 268), it is incorrect to draw the line on the basis of the effect that a particular practice may be said to have on premium charges or insurance benefits. See also pages 16-19, *supra*. The appropriate principles, in our view, may be summarized as follows: If two or more insurance companies agree on the premiums to be charged for insurance or on the benefits to be paid for a given insured loss, such agreements are part of the "business of insurance" and are ordinarily immune from antitrust scrutiny (if they are regulated by state law). If individual insurers then enter into contracts with suppliers or providers solely for the purpose of implementing a lawful agreement among the insurers, those contracts are lawful but not immune. They are lawful not because the provider contracts are also part of "the business of insurance" or because they have a "vital impact on [insurance] rates," but simply because they

are lawful under standard antitrust analysis. But if the provider contracts have some other purpose or effect that is unlawful under the antitrust laws (*e.g.*, to fix prices or reduce competition in the provider market, as alleged in this case), then their lack of immunity becomes important, and antitrust scrutiny is appropriate.²¹

²¹ Indeed, we suggest that the opinion in *Proctor* reflects much of our analysis. It seems likely that the court's conclusion on immunity was based more on its view of the antitrust merits of the complaint than on whether an agreement between an insurer and a supplier of goods or services is the business of insurance. Thus the court stated (561 F. 2d at 268 n. 10):

It is not contended that [the insurers'] effort to give business to some shops, and take away business from other shops, was motivated by reasons independent of the prices charged by those shops. Nor is it alleged that [the insurers] were trying to drive existing body shops out of business in order to facilitate vertical integration by insurance companies into the auto repair industry. We therefore need not decide whether the presence of such factors would have placed the disputed activities outside the business of insurance.

That statement suggests that if the complaint states a meritorious antitrust complaint, or the proof establishes it, the transaction is not in the "business of insurance." We do not agree with a method of analysis that makes immunity turn on the merits of the antitrust complaint (see pages 10-11, *supra*), but the court of appeals' approach may explain much of its immunity discussion that otherwise appears to be at odds with our submission.

4. The labor immunity cases

This Court's decisions concerning the somewhat analogous antitrust exemptions provided to labor unions and their collective bargaining activities by Sections 6 and 20 of the Clayton Act, 38 Stat. 731, 738, 15 U.S.C. 17²³ and 29 U.S.C. 52, and the Norris-LaGuardia Act, 47 Stat. 70, 71, 73, 29 U.S.C. 104, 105, 113, support our position here. It is well established that those statutory exemptions shield labor organizations and employers from antitrust liability with respect to negotiations and agreements between unions and employers (or employer groups) about wages and other conditions of employment. But those exemptions do not apply to agreements between unions and employers that are designed to restrain competition among employers—for example, to fix prices in the employers' market or to drive certain employers out of business—even if such agreements are embodied in collective bargaining agreements and may redound to the benefit of some workers by enabling the employers to pay higher wages. *Connell Construction Co. v. Plumbers & Steamfitters*, 421 U.S. 616; *Ramsey v. United Mine Workers*, 401 U.S. 302, 313; *United Mine Workers v. Pennington*, 381 U.S. 657,

²³ Section 6 of the Clayton Act, 15 U.S.C. 17, provides in pertinent part:

*** Nothing contained in the antitrust laws shall be construed to forbid the existence and operation of labor *** organizations *** or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof ***.

664-665; *Allen Bradley Co. v. International Brotherhood of Electrical Workers*, 325 U.S. 797, 807.²⁴ As the Court said in *Pennington*, *supra*, 381 U.S. at 665-666 (footnote omitted):

[A] union may make wage agreements with a multi-employer bargaining unit and may in pursuance of its own union interests seek to obtain the same terms from other employers. No case under the antitrust laws could be made out on evidence limited to such union behavior. But we think a union forfeits its exemption from the antitrust laws when it is clearly shown that it had agreed with one set of employers to impose a certain wage scale on other bargaining units. One group of employers may not conspire to eliminate competitors from the industry and the union is liable with the employers if it becomes a party to the conspiracy.^[24]

The same principles, we believe, apply to the "business of insurance" exemption under the McCarran-

²⁴ *Mackey v. National Football League*, 543 F. 2d 606, 612 (C.A. 8), certiorari dismissed, 434 U.S. 801, and other cases cited by petitioners (Br. 36), are not to the contrary. They merely recognize that, if an agreement is exempted from the antitrust laws by the labor exemptions, neither party to the agreement is liable under the antitrust laws. They also recognize, however, that both the union and employer groups lose any immunity when the union conspires with employers for the purpose of restraining trade in the employer industry.

²⁵ The same principles have been applied in the case of the antitrust exemption for agricultural organizations under Section 1 of the Capper-Volstead Act, 42 Stat. 388, 7 U.S.C. 291. *Case-Swayne Co., Inc. v. Sunkist Growers, Inc.*, 389 U.S. 384, 395; *National Broiler Marketing Association v. United States*, No. 77-117, decided June 12, 1978, slip op. 6 n. 11.

Ferguson Act, although the statutory exemption is cast in somewhat different terms. When insurers agree among themselves about matters concerning the relationship between insurers and insureds, the McCarran-Ferguson Act exempts such agreements from the antitrust laws to the extent they are regulated by state law and to the extent they do not constitute "boycott, coercion, or intimidation" within the meaning of Section 3(b). But agreements between insurance companies and other entities that restrain competition outside the insurance market are no more entitled to antitrust immunity than union-employers agreements designed to force certain employers out of business or to fix the price of goods and services other than wages and conditions of employment. In either case, the fact that such an agreement may affect wages (or insurance premiums) because it affects the flow of income to the employer (or insurer) is irrelevant.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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JULY 1978.